University of Miami Business Law Review

6-1-2016

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The pari passu clause is found in nearly every sovereign debt contract issued throughout the globe. In the private context, this clause is well understood to ensure fair distributions to all creditors in the event of bankruptcy and liquidation. As insolvency distributions are not an option when dealing with distressed sovereign debt, the rights and duties associated with this clause have been subject to extensive litigation for over 20 years.

Starting from the case of Elliot v. Peru, in the early 1990s, and more recently in Argentina v. NML, courts have interpreting these bonds, governed subject to New York law, in favor of holdout creditors. By means of a novel interpretation of the clause, vulture funds have gained a legal "weapon" with which they can force a sovereign nation into default if they are not paid in full. As a result, sovereign debtors have rapidly begun to adapt the pari passu clause in their new debt contracts to negate the adverse position of the courts. This leads to the questions of why these contracts have been so slow to adapt and what catalyst has been the impetus of change in recent years.

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I. INTRODUCTION

What happens when a country can no longer meet its debt obligations? For individuals, corporations, and municipalities, when a person or entity cannot repay its debts, bankruptcy may be the next step.[1] Bankruptcy allows the debtor either to liquidate, by surrendering its assets to creditors, or to restructure the debt.[2] Even if an individual does not file for bankruptcy, the bankruptcy laws governing liquidation and reorganization will provide the legal backdrop against which an out-of-court workout may be reached.[3] Creditors who might otherwise oppose a debt restructuring may ultimately consent, knowing that a court could force a restructuring over their objections.[4] For a sovereign, however, there is no bankruptcy option.[5] There are no procedures for liquidating a

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1 *See* 11 U.S.C. § 109 (2014).

2 UNITED STATES COURTS, http://www.uscourts.gov/FederalCourts/Bankruptcy/BankruptcyBasics/Process.aspx (last visited Feb. 10, 2015); *see also* 11 U.S.C. (2010). Chapter 7 provides for liquidation of debtor's assets. *Id.* Chapter 9 provides for municipal reorganization. *Id.* Chapter 11 provides for commercial reorganization. *Id.* Chapter 13 provides for adjustment of debts to meet a payment plan for a debtor with regular income. *Id.*

3 *See* Richard M. Cieri et al., *Restructuring bond debt in the global marketplace*, GIBSON DUNN (2004/05), http://www.gibsondunn.com/fstore/documents/pubs/Restructuring_Bond_Debt.pdf, at 33-34.

4 *Id*. at 38-39.

5 *See* Nouriel Roubini, *Gouging the Gauchos*, KITCO (Jul. 01, 2014, 12:18 PM), http://www.kitco.com/ind/Roubini/2014-07-01-Gouging-the-Gauchos.html?sitetype=fullsite#.U7PcQuFRKrg.email [hereinafter Roubini]. In 2002, the IMF proposed a framework for a sovereign bankruptcy court. However, this proposal has been widely considered

sovereign, and there is no background set of legal rules under which a court may "cram down" a debt restructuring.[6]

Without a bankruptcy option, sovereign debt restructuring is vulnerable to holdout problems: a minority of creditors may oppose the terms of a restructuring in order to extract a greater dividend from the sovereign.[7] In order to aid the process of sovereign debt workouts and the restructuring of debt, "boilerplate"[8] language has developed in sovereign debt contracts.[9] While boilerplate language in these contracts serves the general function of standard terms, such as to create a consistent framework familiar to all market participants, certain clauses have been developed specifically to address the holdout problem.[10]

An example of such a boilerplate provision is the collective action clause ("CAC").[11] The market has gradually shifted from unanimous action clauses ("UACs"), which require unanimous creditor approval for debtors to amend bond terms, to CACs, which only require a majority, usually a supermajority,[12] of the other creditors to have accepted the debt's new terms.[13] Thus, CACs allow debtors to "cram down on holdouts . . . terms accepted by a majority of creditors."[14]

Another notable boilerplate clause found in sovereign debt contracts is known as the "pari passu" clause. Pari passu literally means "on equal

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politically infeasible. *See* Jefferey A. Frankel, *Comment on "Toward a Statutory Approach to Sovereign Debt Restructuring: Lessons from Corporate Bankruptcy Practice Around the World"*, IMF (2003), http://www.imf.org/external/pubs/ft/staffp/2002/00-00/pdf/Frankel.pdf, at 78.

6 *See* Roubini, *supra* note 5.

7 *See id*.

8 Boilerplate is "[f]ixed or standardized contractual language that the proposing party often views as relatively nonnegotiable." BOILERPLATE, BLACK'S LAW DICTIONARY (10th ed. 2014).

9 *See* Roubini, *supra* note 5.

10 Stephen J. Choi & G. Mitu Gulati, *Innovation in Boilerplate Contracts: An Empirical Examination of Sovereign Bonds*, 53 EMORY L.J. 929, 930-32 (2004); *see also* Roubini, *supra* note 5.

11 *See* Roubini, *supra* note 5.

12 Supermajority is "[a] fixed proportion greater than half (often two-thirds or a percentage greater than 50%), required for a measure to pass. Such a majority is needed for certain extraordinary actions, such as ratifying a constitutional amendment or approving a fundamental corporate change." MAJORITY, BLACK'S LAW DICTIONARY (10th ed. 2014).

13 *See* Stephen J. Choi et al., *The Dynamics of Contract Evolution*, 88 N.Y.U. L. REV. 1, 13-15 (2013).

14 Roubini, *supra* note 5. Note that even CACs are not a perfect way to avoid a holdout problem in the future. A cramdown is a concept in bankruptcy law where "despite the opposition of certain creditors . . . .a court may confirm a [bankruptcy] plan." CRAMDOWN, BLACK'S LAW DICTIONARY (10th ed. 2014).

footing."[15] The purpose of this clause is to obligate the debtor to treat all creditors fairly by not favoring one creditor through the subordination of another creditor's debt.[16] In the corporate context, this means "those whose debts rank pari passu will get paid on an equal priority in the event of an insolvency distribution."[17] However, as sovereign nations cannot be liquidated, the actual meaning of the pari passu clause in the sovereign debt context has been subject to much dispute.[18] Originally, this clause was thought to protect only the legal "ranking" of a sovereign creditor's claims.[19] However, an interpretation requiring "ratable payment" to creditors appeared with the introduction of litigation on the issue.[20]

The first major case that addressed the clause was *Elliott v. Peru*, a case interpreting the meaning of pari passu as governed by New York law.[21] Elliott Associates L.P., a vulture fund,[22] purchased a large amount

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15 Mark L.J. Wright, *Interpreting the Pari Passu Clause in Sovereign Bond Contracts: It's all Hebrew (and Aramaic) to Me*, FEDERAL RESERVE BANK OF CHICAGO (May 4, 2014), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=24326711, at 1.

16 Lee C. Buchheit & Jeremiah S. Pam, *The Pari Passu Clause in Sovereign Debt Instruments*, 53 EMORY L.J. 869, 911-12 (2004).

17 Stephen J. Choi & G. Mitu Gulati, *Contract as Statute*, 104 MICH. L. REV. 1129, 1134 (2006).

18 *See id.* at 1133-34.

19 *Strengthening the Contractual Framework to Address Collective Action Problems in Sovereign Debt Restructuring*, IMF (Oct. 2014), http://www.imf.org/external/np/pp/eng/2014/090214.pdf at 38 [hereinafter IMF]. This is known as the "ranking" interpretation.

> A sovereign could affect the legal ranking of such creditor claims . . . by (i) earmarking government revenues or by allocating foreign currency reserves to a single creditor, (ii) adopting legal measures that would have the effect of preferring one set of creditors over others, or (iii) allowing creditors to obtain priority without the consent of other creditors.

Id.

20 *Id*. This is known as the "ratable payment" interpretation. *Id.* Under this broader "ratable payment" interpretation, the clause not only protected legal rank, but also included a payment obligation that required the sovereign to pay its creditors on a ratable basis. While this interpretation would not preclude a sovereign from contracting debts with different repayment profiles, the implication was that if the sovereign were unable to pay all of its debts in full as they became due and payable, it would need to pay such debts on a ratable basis.

21 *See* Choi, *supra* note 17 at 1134; *see also* Elliott Associates, L.P. v. Banco de la Nacion, 194 F.3d 363, 366 (2d Cir. 1999).

22 A "vulture fund" is a hedge fund or private equity fund that invests in debt that is considered weak and/or in imminent default (otherwise known as "distressed debt"). "These plaintiffs are often referred to as 'vulture funds' because their strategy is to buy sovereign debt instruments when a country is most vulnerable, which enables the funds to purchase the debt at a deep discount from its face value and attempt to enforce the full claims." Jonathan I. Blackman & Rahul Mukhi, *The Evolution of Modern Sovereign Debt*

of distressed Peruvian bank debt, which was guaranteed by Peru's government.[23] Elliott refused to participate in the restructuring process when the government of Peru could no longer meet its debt obligations, and the fund demanded full repayment of its debt.[24] Despite Elliot's demands, Peru decided to proceed with repaying its creditors that had accepted its new repayment plan.[25] Elliott responded by trying to enjoin European payment processers from assisting Peru by arguing that the pari passu clause prevents debtors from making payments to only some creditors at the exclusion of others—the ratable payment interpretation.[26] This case went before the Belgian Court of Appeals, which sided with Elliott's position.[27] Before the case proceeded to further litigation, the parties settled out of court.[28]

A more recent case that addressed the meaning of the pari passu clause in the sovereign debt context is *Argentina v. NML*.[29] NML Capital,[30] also a vulture fund, acquired a small percentage of Argentina's distressed debt, which was governed by New York law.[31] Later, when Argentina tried to repay its creditors that accepted its restructured debt, NML obtained injunctive relief in the Second Circuit prohibiting Argentina from repaying 93% of its distressed debt to renegotiated bondholders without repaying the remaining 7% to holdout investors simultaneously.[32] The Court's adoption of the ratable payment interpretation forced Argentina to default on its restructured bonds and effectively gave a hedge fund the power to control a country's ability to repay its debts, by preventing the country from repaying its renegotiated bondholders until the holdout creditors' debts were satisfied.[33]

Litigation: Vultures, Alter Egos, and Other Legal Fauna, 73 LAW AND CONTEMPORARY PROBLEMS 47, 49 (Fall 2010), http://scholarship.law.duke.edu/lcp/vol73/iss4/6/.

23 Umakanth Varottil, *Sovereign Debt Documentation: Unraveling the Pari Passu Mystery*, 7 DEPAUL BUS. & COM. L.J. 119, 120 (2008).

24 *See id.*

25 *See id.* at 121.

26 *See id.* at 121-22.

27 *Id.* at 122.

28 *Id.*

29 *See* IMF, *supra* note 19, at 40-41.

30 It is interesting to note that NML Capital, the plaintiff in the *Argentina* litigation, is a subsidiary of Elliott Associates, the plaintiff in the *Peru* litigation. *See Africa and Latin America Still Fight Vulture Funds*, THE WORLD POST (Nov. 12, 2012, 2:46 PM), http://www.huffingtonpost.com/hector-timerman/africa-latin-america-vulture-funds_b_2100827.html.

31 *See* IMF, *supra* note 19, at 8.

32 *Id.* at 8-9.

33 *See* Roubini, *Supra* note 5; *see also* Jamila Trindle, *Argentine Default Bad Test Case for Sovereign Debt Negotiations*, FOREIGN POLICY (Aug. 25, 2014), http://www.foreignpo

As a reaction to the recent *Argentina* decision,[34] there has been a sudden urgency to avoid a similar holdout investor problem in the future by rewording the boilerplate language in sovereign debt contracts.[35] Both the International Capital Markets Association ("ICMA") and the International Monetary Fund ("IMF") have been very involved with reworking these contracts.[36] Besides making changes to the pari passu clause, the CACs for new bond contracts have also been reworked.[37]

The sudden urgency to change the boilerplate language of sovereign debt contracts begs the question: why did the boilerplate language not change after *Elliott v. Peru* in contrast to the rapid change now taking place after *Argentina v. NML*? Phrased differently, boilerplate language is known to be "sticky" and is not changed very often.[38] By using standardized terms, contracting parties are able to lower uncertainty levels and reduce contracting costs.[39] What then changed that is leading to this language being modified so quickly now?

This Comment argues that after *Argentina*, the pari passu clause became a "weapon" that holdout investors could use. Unlike after *Peru*, holdout investors such as hedge funds, are empowered to, and have, forced a sovereign nation to default on its debt after Argentina. In *Peru*, the danger of the Belgian Court's interpretation of the pari passu clause was recognized, but no harm ultimately arose and the decision was considered a one-off occurrence. The nature of the Second Circuit's *Argentina* ruling and the subsequent Argentina default is so extreme that it has dictated a market response that differs in severity and speed from *Peru*. Also, unlike the typical slow adoption of new boilerplate terms by market participants, a much quicker and broader large-scale adoption may be expected.

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licy.com/articles/2014/08/25/argentina_default_bond_vulture_hedge_fund_sovereign_debt_grenada.

[34] The Second Circuit issued its decision in October 2012. However, its decision was not final until the Supreme Court refused to hear Argentina's appeal in June 2014. *See infra* p. 16.

[35] *See, e.g.,* Anna Gelpern, *A Sensible Step to Mitigate Sovereign Bond Dysfunction*, PETERSON INSTITUTE FOR INTERNATIONAL ECONOMICS (Aug. 29, 2014, 4:57 PM), http://blogs.piie.com/realtime/?p=4485; *see also* IMF, *supra* note 19, at 8-9.After the Supreme Court decision came out in June 2014, ICMA and the IMF published proposed amendments to the clauses within months—August and October respectively. *Id.*

[36] *See* Gelpern, *supra* note 35; *see* IMF, *supra* note 19.

[37] *See generally* IMF, *supra* note 19, at 15-30.

[38] Gregory H. Shill, *Boilerplate Shock: Sovereign Debt Contracts as Incubators of Systemic Risk*, 89 TUL. L. REV. 751, 765 (2015).

[39] Choi, *supra* note 10, at 931.

Part II of this Comment describes the nature of sovereign debt boilerplate contracts and narrates events, both during and following *Elliot v. Peru* and *Argentina v. NML*. Parts III and IV of this Comment then explain the reasons for the differing market responses, describe what type of further litigation of the pari passu clause may arise, and briefly examine what to expect should the interpretation of the pari passu clause be challenged as a matter of English law.

II. BACKGROUND

A. The Nature of Sovereign Debt Boilerplate

Two types of provisions in sovereign debt contracts are particularly important as to the holdout creditor problem—the pari passu clause and the collective action clause ("CAC"). The pari passu clause has existed as boilerplate language in sovereign debt contracts for nearly two centuries.[40] This clause arguably empowers creditors by preventing debtors from subordinating one creditor's claim to another creditor's claim.[41] CACs are a more recent development designed specifically to address the holdout problem by empowering the debtor.[42] After bonds are issued, parties require a way to restructure debt outside of a bankruptcy court.[43] Thus, unanimous action clauses ("UACs") and CACs were included in bond contracts to allow parties to amend terms of the bond issue.[44] UACs require unanimous bondholder approval in order to modify principal and interest terms of the contract.[45] In contrast, CACs serve a similar purpose, but do not require unanimous approval, making it easier to reduce the payment terms in sovereign bonds.[46] With no other way to "cram down" new terms on holdouts of sovereign debt contracts, as bankruptcy is not an option, CACs are increasingly employed.[47]

Much research on sovereign debt boilerplate has focused on the shift from UACs to CACs in sovereign bonds.[48] The shift to CACs began in late 2000, when Ecuador used a creative interpretation of a UAC clause

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40 Benjamin Remy Chabot & Mitu Gulati, *Santa Anna and His Black Eagle: The Origins of Pari Passu?*, 9 CAPITAL MARKETS LAW JOURNAL 1, 1 (Feb. 18, 2014), http://scholarship.law.duke.edu/faculty_scholarship/3237/.

41 *See* Choi, *supra* note 17, at 1133-36.

42 Roubini, *supra* note 5.

43 *See* Choi, *supra* note 10, at 932.

44 *Id*.

45 *Id*.

46 *See id.*

47 Roubini, *supra* note 5.

48 *See* Choi, *supra* note 10, at 932.

to modify existing bond terms with less than unanimous approval from bondholders.[49] Ecuador structured an exchange offer where bondholders who participated in the exchange automatically voted in favor of a list of amendments to the old bonds; thus, making those bonds less attractive to holdout investors.[50] This restructuring method effectively reduced incentives for holdout investors to refrain from participating in the bond exchange in the hope that they would be able to negotiate for better terms at a later date.[51] However, it took three years for the market to shift away from existing UAC terms and to begin using modified CACs—only after Mexico took the first step by redrafting its consent clauses.[52]

Stephen Choi and Mitu Gulati, two of the preeminent scholars on the nature of boilerplate language in sovereign debt contracts, attributed the lack of an immediate shift to new contract terms to the "stickiness hypothesis."[53] The standardized nature of sovereign debt contracts has been attributed to network externalities.[54] No meaningful regulatory body exists that interferes with the contracting practices of such contracts.[55] Further, such contracts involve hundreds of millions of dollars and are often traded in the secondary market.[56] Thus, adopting standardized terms in these contracts helps lower uncertainty levels and reduces

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49 Choi, *supra* note 10, at 933; *see also* Policy Development and Review and Legal Departments, *Involving the Private Sector in the Resolution of Financial Crises—Restructuring Internationals Sovereign Bonds*, IMF (Jan. 24, 2001), http://www.imf.org/external/pubs/ft/series/03/IPS.pdf at 7 [hereinafter IMF, Policy Development].

50 IMF, Policy Development, *supra* note 49, at 8. The amendment deleted:

> the requirement that all payment defaults must be cured as a condition to any rescission of acceleration, the provision that restricts Ecuador from purchasing any of the Brady bonds while a payment default is continuing, the covenant that prohibits Ecuador from seeking a further restructuring of Brady bonds, the cross-default clause, the negative pledge covenant, and the covenant to maintain the listing of the defaulted instruments on the Luxembourg Stock Exchange.

Id.

51 *Id.*

52 *See* Omri Ben-Shahar & John A. E. Pottow, *On the Stickiness of Default Rules*, 33 FLA. ST. U. L. REV. 651, 681 (2006).

53 *Id.*

54 Choi, *supra* note 10, at 930-31. The discussion of network externalities originated in economic theory. Bryan Druzin, *Buying Commercial Law: Choice of Law, Choice of Forum, and Network Externalities,* 18 TUL. J. INT'L & COMP. L. 131, 145 (2009). "[T]he notion of network externalities . . . has been put forward as a way of explaining the ascendancy of particular products over others." *Id.* "Positive feedback mechanisms . . . reinforce bourgeoning patterns in a particular field, causing these patterns to become progressively more entrenched." *Id*. at 146.

55 Choi, *supra* note 10, at 930.

56 *Id.*

contracting costs.[57] A change in sovereign debt contracts only occurs when there is an "interpretive shock."[58] This change is typically not immediate, and will usually only take place in small shifts.[59] Debtors avoid making a large shift due to the uncertainty that the new contract terms are any better, and will usually wait for these deviance costs to be borne by a "pioneer."[60]

B. Litigation Involving Pari Passu—Two Interpretations

Recently, much litigation of sovereign debt boilerplate has focused on the pari passu clause.[61] Numerous scholars have posited various theories as to why this clause was first introduced.[62] Despite the fact that the clause has been found in nearly every single sovereign debt contract since its introduction, there is no one accepted understanding as to its meaning.[63]

A typical pari passu clause is worded as such: "The Notes rank, and will rank, *pari passu* in right of payment with all other present and future unsecured and unsubordinated External Indebtedness of the Issuer."[64]

Pari passu roughly translates to "on equal footing."[65] In the case of corporate bonds, commentators have widely agreed on the meaning of this clause: that in the event of insolvency and liquidation, all holders of equally ranked debt will receive an equal share of the proceeds.[66] However, in the sovereign debt context, there is no option of liquidation

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57 *Id.* at 931.

58 *See* Choi, *supra* note 10, at 946.

59 *See id.* at 945-46.

60 *Id.*; Ben-Shahar, *supra* note 52, at 681.

61 IMF, *supra* note 19, at 38.

62 *See, e.g.*, Buchheit, *supra* note 16, at 875.

> These explanations have ranged from a suggestion that drafters may have wanted to prevent an informal 'earmarking' of a sovereign's assets or revenues to service a particular debt to the more cynical explanation that this type of debt had a tendency to migrate—through the ignorance or inattention of contract drafters—from cross-border corporate debt instruments to sovereign debt instruments.

Id.; *see also* Chabot, *supra* note 40, at 2 ("Santa Anna and his Equal Treatment Decree"); *see also* Wright, *supra* note 15; *see also* Mark C. Weidemaier et al., *Origins Myths, Contracts, and the Hunt for Pari Passu*, 38 Law and Soc. Inquiry 72 (Mar. 25, 2011), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1633439.

63 *See* Chabot, *supra* note 40, at 2.

64 Buchheit, *supra* note 16, at 871 (emphasis added).

65 Wright, *supra* note 14, at 1.

66 Weidemaier, *supra* note 52, at 4; *see also* Choi, *supra* note 17, at 1134.

in the event of insolvency.[67] Thus, the actual legal implications of this clause under such circumstances are not clearly understood.[68]

1. Elliott V. Peru

"Until the late 1990s, the prevailing view was that the typical *pari passu* clause in sovereign debt agreements protected only the legal ranking of a sovereign's creditors."[69] Before then, this clause was thought to prevent the subordination of one creditor's debt to another without the other creditor's consent.[70] For example, in some countries, such as Spain and the Philippines, the act of notarizing a debt renders it senior to other debts that have not been notarized.[71] Thus, the pari passu clause prevented such involuntary subordination and provided security to creditors in cross-border transactions.[72]

However, "in the late 1990s, an alternative interpretation of the *pari passu* clause as requiring 'ratable payment' to creditors surfaced in litigation against sovereign debtors."[73] This new interpretation of pari passu was introduced in a case brought by the investment fund Elliott Associates, L.P.[74]

Between January and March 1996, Elliott purchased approximately $20.7 million of working capital debt of Banco de la Nacion and Banco Popular del Peru, a bankrupt Peruvian bank.[75] "[A]ll of the debt was guaranteed by Peru pursuant to a written guaranty dated May 31, 1983," which was governed by New York law.[76] Despite Peru's attempts to restructure this debt, Elliott refused to participate in the restructuring process.[77] Elliott pursued and obtained judgment in the Southern District of New York for over $55 million.[78] Despite its win, Elliott faced the difficulty of actually collecting the judgment.[79] Peru decided to repay the

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67 Weidemaier, *supra* note 52, at 4.
68 *Id.*
69 IMF, *supra* note 19, at 38.

70 *Id.*
71 *Id.* at 37 n. 2.
72 *See id.* at 37.
73 *Id.* at 38.
74 *ISSUE 79—PARI PASSU CLAUSES*, 79 FINANCIAL MARKETS LAW COMMITTEE 1, 8 (Mar. 2005), http://ftalphaville.ft.com/files/2012/11/fmlc79mar_2005.pdf [hereinafter FMLC].
75 Elliott Associates, L.P. v. Banco de la Nacion, 194 F.3d 363, 366-67 (2d Cir. 1999).
76 *Id.* at 367.
77 Varottil, *supra* note 23, at 120.
78 *Id.* at 120-21.
79 *Id.* at 121.

holders of its restructured Brady Bonds,[80] by using the Euroclear System in Belgium, and to avoid the payment due to Elliott.[81] In September 2000, Elliott attempted to enforce its judgment by seeking an injunction in the Belgian Courts to prevent Euroclear from processing Peru's payment.[82]

In an affidavit obtained by Elliott for the purpose of the Peru litigation, New York University Professor Andreas Lowenfeld explained the pari passu clause as such:

> I have no difficulty in understanding what the pari passu clause means: it means what it says—a given debt will rank equally with other debt of the borrower, whether that borrower is an individual, a company, or a sovereign state. A borrower from Tom, Dick, and Harry can't say "I will pay Tom and Dick in full, and if there is anything left over I'll pay Harry." If there is not enough money to go around, the borrower faced with a pari passu provision must pay all three of them on the same basis.
>
> Suppose, for example, the total debt is $50,000 and the borrower has only $30,000 available. Tom lent $20,000 and Dick and Harry lent $15,000 each. The borrower must pay three fifths of the amount owed to each one – *i.e.*, $12,000 to Tom, and $9,000 each to Dick and Harry. Of course the remaining sums would remain as obligations of the borrower. But if the borrower proposed to pay Tom $20,000 in full satisfaction, Dick $10,000 and Harry nothing, a court could and should issue an injunction at the behest of Harry. The injunction would run in the first instance against the borrower, but I believe (putting jurisdictional considerations aside) to Tom and Dick as well.[83]

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80 Brady Bonds are named after former U.S. Treasury Secretary Nicholas Brady. These bonds were introduced in the late 1980s to address the Latin Debt Crisis, when a number of Latin American countries admitted their inability to service hundreds of billions of dollars worth of commercial bank loans. In exchange for the commercial bank loans, the countries issued new bonds with more agreeable repayment terms. This plan was largely successful. *See The Brady Plan*, EMTA, http://www.emta.org/template.aspx?id=35&terms=brady+plan (last visited Feb. 12, 2015).

81 IMF, *supra* note 19, at 38-39.

82 *Id.*

83 Buchheit, *supra* note 16, at 878. This affidavit was a key element of Peru's case. *See id.*

The Belgian Court of Appeals accepted this interpretation of pari passu and held that a sovereign debtor cannot make payments to one creditor to the exclusion of other creditors.[84] The Belgian Court's decision prevented Peru from paying the holders of its restructured debt, and Peru subsequently settled with Elliott.[85]

2. After Peru

It is important to note that after the Belgian Court's decision in the *Peru* case, the language of the pari passu clause in sovereign debt contracts did not change.[86] In an attempt to understand this lack of market response, Choi and Gulati conducted "over fifty in-depth interviews with market participants" to try and discern the reason for this lack of response.[87] The most meaningful reason that Choi and Gulati could identify was "that it was impossible for standard-form clauses that were present in every single sovereign debt instrument across the globe to change every time there was an aberrant court decision."[88]

Instead of focusing on contractual language, the market did eventually produce a coordinated response to *Peru* in a different form.[89] In 2003, the sovereign debt community organized itself around a general litigation strategy and attempted to protect the "ranking" interpretation of the pari passu clause when the issue surfaced in U.S. courts.[90] The contested interpretation of the pari passu clause appeared in a New York court in a case regarding the restructuring of Argentina's sovereign debt.[91]

3. Argentina V. NML

In 2001, Argentina defaulted on its Fiscal Agency Agreement Bonds ("FAA Bonds"),[92] which were originally issued in 1994, and "declared a

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84 *See* Varottil, *supra* note 23, at 121-22.
85 *Id.* at 122.
86 *See* Choi, *supra* note 17, at 1137.
87 *Id.* at 1136-37.
88 *Id.* at 1137-38.
89 *See id.* at 1138.
90 *See id.*
91 *Id.*
92 These FAA Bonds were Brady Bonds. A fiscal agency agreement operates where a fiscal agent acts as a trustee for bondholders to receive funds from the debtor and make payments of interest and principal accordingly. "The Agreement further obligates the fiscal agent to give notice to bondholders . . . [i]f the debtor fails to deposit sufficient funds to pay the interest due[,] if a bondholder claims that an 'event of default' or 'default' occurred[,] or if the bonds have ever been accelerated." Rory Macmillan, *The Next Sovereign Debt Crisis*, 31 Stan. J. Int'l L. 305, 341-42 (1995).

'temporary moratorium' on principal and interest payments . . . ."[93] These bonds contained what the court called an "Equal Treatment Provision"—namely, the pari passu clause.[94] Following its default, in 2005, Argentina offered to exchange the FAA Bonds for new bonds with different terms.[95] Subsequently, Argentina renewed the moratorium, which halted all payments on the FAA Bonds.[96] In 2010, Argentina again renewed its offer to exchange the bonds.[97]

The plaintiffs in the case, NML Capital, owned defaulted FAA bonds.[98] NML sued Argentina, alleging breach of contract under the pari passu clause, and sought injunctive relief for specific performance of the Equal Treatment Provision.[99] "In February 2012, the district court granted injunctive relief, ordering Argentina to specifically perform its obligations under the Equal Treatment Provision . . . ."[100] On appeal, in October 2012, the Second Circuit affirmed the district court's decision granting summary judgment to NML Capital on their claim for breach of the pari passu clause, and ordered Argentina to make "ratable payments" to all holders of its debt.[101] Yet, the Second Circuit stayed the injunctive relief until the Supreme Court heard Argentina's appeal.[102] In June 2014, the Supreme Court refused to hear Argentina's appeal, and the Second Circuit lifted the prior stay on the injunctions.[103] Thus, Argentina found itself unable to pay its creditors holding restructured bonds without paying its holdout investors in full under the Second Circuit's ratable payment order.[104]

Following the Supreme Court's decision, Argentina failed to make a $539 million payment that was due on its debts by July 2014.[105] This move led ratings-agency-Fitch to declare Argentina's sovereign debt in "restricted default."[106]

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93 NML Capital, Ltd. v. Republic of Argentina, 699 F.3d 246, 251 (2d Cir. 2012).
94 *Id.*
95 *Id.* at 252.
96 *See id.* at 251.
97 *Id.* at 252.
98 NML Capital, Ltd. v. Republic of Argentina, 699 F.3d 246, 253 (2d Cir. 2012).
99 *Id.*
100 *Id.* at 254.
101 *Id.* at 265.
102 IMF, *supra* note 19, at 9.
103 *Id.*
104 *Id.* at 4.
105 *Argentina downgraded to 'restricted default': Fitch*, FASTFT, http://www.ft.com/intl/fastft/189422/fitch-downgrades-argentina-restricted-default (last visited Feb. 12, 2015) [hereinafter Fitch].
106 *Id.*; Fitch assigns a "restricted default" rating when an issuer "has experienced an uncured payment default on a bond, loan or other material financial obligation but which has not entered into bankruptcy filings, administration, receivership, liquidation or other

Effectively, the collective decisions of the U.S. courts gave a hedge fund the power to force a sovereign nation to default on its debts—a power that was actually used. Accordingly, there is no longer any incentive for creditors, in future sovereign debt out-of-court workouts, to accept reduced terms when they have the legal means to insist on payment in full.[107]

4. After Argentina

In response to the Second Circuit's and Supreme Court's decisions in *Argentina v. NML*, there has been a sudden urgency for contract reform in the area of sovereign debt.[108] "On August 29, 2014, the International Capital Market Association (ICMA) released a new set of model clauses for sovereign bond contracts to address some of these flaws."[109] ICMA has proposed clarifying and standardizing the pari passu clause to prevent courts from ordering debtors to pay holdout investors whenever the debtors are paying holders of restructured debt.[110]

In addition, the International Monetary Fund ("IMF") has published a policy paper examining potential areas of reform in the contractual framework of sovereign bonds, which particularly addresses the need to modify the pari passu clause.[111] The IMF has explained that the new model clauses "make explicit that, while it requires equal ranking of all unsubordinated external indebtedness, it does not require that such indebtedness be paid on an equal or ratable basis."[112]

Changes to the boilerplate terms in sovereign debt contracts have not been limited to theoretical discussions alone.[113] Peru, Mexico, Kazakhstan, and Vietnam have all filed registration statements with the

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formal winding-up procedure, and which has not otherwise ceased operating." *Definitions of Ratings and Other Forms of Opinion*, FITCH RATINGS (Dec. 2014), https://www.fitchratings.com/web_content/ratings/fitch_ratings_definitions_and_scales.pdf, at 34.

107 Roubini, *supra* note 5.

108 *See, e.g.,* Roubini, *supra* note 5; *see also* Gelpern, *supra* note 35; *see also* IMF, *supra* note 19; *see also* Anna Gelpern, *ICMA CACs v. 2.0: Mexico Moves in New York*, CREDIT SLIPS (Nov. 10, 2014, 11:51 PM), http://www.creditslips.org/creditslips/2014/11/icma-cacs-v-20-mexico-moves-in-new-york.html [hereinafter Gelpern, *CACs v. 2.0*]; *see also* Anna Gelpern, *ICMA CACs, New York Edition—Vietnam!—and more Un-Boilerplate*, CREDIT SLIPS (Nov. 18, 2014, 11:13 AM), http://www.creditslips.org/creditslips/2014/11/icma-cacs-new-york-edition-vietnam-and-more-un-boilerplate.html [hereinafter Gelpern, *ICMA CACs*].

109 Gelpern, *supra* note 35.

110 *Id.*

111 *See* IMF, *supra* note 19, at 4.

112 *Id.* at 15.

113 *See, e.g.,* Gelpern, *CACs v. 2.0*, *supra* note 108; *see also* Gelpern, *ICMA CACs*, *supra* note 108.

SEC that reflect the proposed terms of the ICMA model clauses.[114] Take for example Mexico's new pari passu clause:

> The debt securities rank and will rank without any preference among themselves and equally with all other unsubordinated public external indebtedness of Mexico. It is understood that this provision shall not be construed so as to require Mexico to make payments under the debt securities ratably with payments being made under any other public external indebtedness.[115]

A notable feature of many of these clauses is that they no longer include the Latin term pari passu and that they explicitly disavow the ratable payment construction.[116] Although they are modeled on the ICMA model clauses, the new pari passu clauses seem to exclude payment in slightly different ways.[117] For example, Kazakhstan's new pari passu clause is phrased as follows:

> The Notes will at all times rank *pari passu* without preference among themselves and at least pari passu in right of payment, with all other unsecured External Indebtedness of the Issuer from time to time outstanding, provided, however, that the Issuer shall have no obligation to effect equal or rateable payment(s) at any time with respect to the Notes or any other External Indebtedness and, in particular, shall have no obligation to pay other External Indebtedness at the same time or as a condition of paying sums due on the Notes and *vice versa*.[118]

And Vietnam's new pari passu clause is phrased as follows:

> The Notes shall at all times rank without any preference among themselves and equally with all other present and future unsecured and unsubordinated External Indebtedness (subject to Condition 11 below [Negative Pledge]) provided, however, consistent with similar provisions in the Government's other External

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114 *See, e.g.,* Gelpern, *CACs v. 2.0*, *supra* note 108; *see also* Gelpern, *ICMA CACs*, *supra* note 108.

115 Gelpern, *ICMA CACs*, *supra* note 108.

116 *See id*.

117 *Id*.

118 *Id*.

> Indebtedness, that this provision shall not be construed so as to oblige the Government to effect equal or rateable payment(s) at any time with respect to any such other External Indebtedness and, in particular, it shall not be construed so as to oblige the Government to pay other External Indebtedness at the same time or as a condition of paying sums due on the Notes and vice versa.[119]

Compared to the new pari passu clauses of Kazakhstan and Vietnam, Mexico's new provision clearly and succinctly states the intended purpose of the contract's clause, therefore, ensuring that a future court will not require payment on a ratable basis—an objective that all three clauses aim to achieve.

III. ANALYSIS

A. Question

Professors Stephen Choi and Mitu Gulati explain that boilerplate clauses in sovereign debt contracts do not change until they receive an "interpretive shock."[120] However, as demonstrated by the cases of *Peru* and *Argentina*, the coordinated market response may take different forms.[121] Following *Peru*, the market reacted with a coordinated litigation strategy.[122] Following *Argentina*, the market reacted swiftly by modifying and adopting new formations of the pari passu clause.[123]

After *Peru*, Choi and Gulati's research revealed that boilerplate clauses do not change "every time there was an aberrant court decision."[124] *Peru* and *Argentina* are very similar decisions, but each case produced a very different reaction.[125] Why then did the response to the "interpretive shock" after *Peru* manifest itself as a litigation strategy as opposed to a contractual drafting strategy?

Furthermore, Choi and Gulati's research has shown that after an "interpretive shock," most countries will not initially change their boilerplate language.[126] Any change will usually be preceded by a

119 *Id*.
120 *See* Choi, *supra* note 10, at 937.
121 Choi, *supra* note 17, at 1139.
122 *Id.* at 1138.
123 *See, e.g.,* Gelpern, *ICMA CACs*, *supra* note 108.
124 Choi, *supra* note 17, at 1137-38.
125 *See generally* IMF, *supra* note 19, at 38-42.
126 *See* Ben-Shahar, *supra* note 52, at 681.

substantial time lag.[127] It took nearly three years before Mexico altered its UACs to reflect the meaning applied by *Ecuador*.[128] In *Peru*, the market only reacted with its litigation strategy when the contested interpretation of the pari passu clause made an appearance in New York courts.[129] Why then did modifications to the pari passu clause appear so rapidly following *Argentina v. NML*?[130] Why was there no waiting period before new contractual clauses were drafted?

B. Answer

In order to understand the reason for the speed of the market response after *Argentina*, we must first understand the reason for the lack of severity in the market response following *Peru*. Why was a litigation strategy seen as a better option than modifying the boilerplate clauses? Explanations of the coordinated market response following *Peru* can be divided in to two groups—endogenous reasons and exogenous reasons.[131]

Endogenous reasons look inward, to the nature of the boilerplate contract itself.[132] Boilerplate contracts are inherently "sticky" in order to lower transaction costs to market participants.[133] Change occurs when the "interpretive shock" itself becomes too costly for market participants.[134] After *Peru*, many market participants believed that the Belgian Court's decision was a one-time occurrence.[135] They doubted that a New York court would accept a similar interpretation.[136] Additionally, a change to contractual terms would be helpful for new contracts, but it would not address the preexisting debt with doubtful pari passu language.[137] The costs involved in reworking the pari passu clause would entail the costs of mass coordination as well as the uncertainty involved with using a

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127 *See id.*
128 *Id.*
129 *See* Choi, *supra* note 17, at 1138.
130 *See generally* Gelpern, *supra* note 35.
131 Varottil, *supra* note 23, at 131-41.
132 *Id.* at 131; *see supra,* p. 10 and notes 53-60.
133 *See* Shill, *supra* note 38, at 765.
134 Varottil, *supra* note 23, at 132.
135 *See* Choi, *supra* note 17, at 1137-38. In Peru, there were numerous reasons to perceive the decision of the court as less significant. *See* IMF, *supra* note 19, at 38-39. First, this was an instance of a foreign court ruling on the interpretation of a clause subject to New York law. *Id.* at 39. Second, the Brussels court granted the restraining order against Euroclear on an ex parte basis. *Id.* Third, Peru ultimately settled with Elliott before the hearing on its motion to vacate the court's order. *Id.*
136 *See* Choi, *supra* note 17, at 1137.
137 *See id.*

non-standard term.[138] Therefore, a coordinated litigation strategy was seen as the most effective way to protect the interpretation of pari passu clauses—both old and new.[139]

Exogenous reasons look to outside factors that, while operating simultaneously, may mitigate the need for change.[140] Around the same time as *Peru*, the market saw a shift from UACs, which required unanimous bondholder approval to make modifications to repayment terms, to CACs, which only required a majority (or sometimes supermajority) of bondholders to agree to modifications.[141] This change gave increased power to sovereign debtors and decreased the power of holdout creditors.[142] Thus, there was less perceived need to further decrease the power of holdout creditors.[143] Also, the 2001 Argentinean debt default occurred shortly after the *Peru* decision.[144] This presented the perfect opportunity for market participants to merely continue the litigation process.

However, *Argentina* differs from *Peru* in one key way—besides giving a holdout investor a "weapon" to use, a holdout investor has actually used said weapon.[145] This case gave private creditors a weapon with which they could enjoin a sovereign debtor's repayment to any other creditor holding debt of the same legal priority.[146] This weapon was then used by NML against Argentina when the fund forced the nation into default.[147] These cases are no longer instances of a vulture fund waving a metaphorical gun; following *Argentina*, NML actually fired the weapon.

Although the Belgian Court decision in *Peru* was also seen as placing a weapon in the hands of holdout investors, the potential weapon was never used, as the parties reached a settlement.[148] Thus, the *Peru* decision raised awareness to the risks associated with the pari passu clause, but it left no major impact.[149] Only after a holdout investor

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138 *See id.* at 1137-38; *see also* Varottil, *supra* note 23, at 133.
139 *See* Choi, *supra* note 17, at 1138-39.
140 Varottil, *supra* note 23, at 134.
141 *Id.* at 136-37.
142 *See id.*
143 *See id.*
144 *See* IMF, *supra* note 19, at 40.
145 *See* Melissa Boudreau & Mitu Gulati ,*The IMF's Imperiled Priority*, 10 DUKE J. CONST. L. & PUB. POL'Y 119, 199 (Jun. 23, 2014), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2458098, at 1.
146 *Id.* at 29.
147 *See* Trindle, *supra* note 33; *see also* Fitch, *supra* note 105.
148 *See* Choi, *supra* note 10, at 991.
149 *See generally* IMF, *supra* note 19, at 40.

exercised its power over a sovereign nation, did the need for rapid change become so clear.[150]

Now, unlike *Peru*, the cost of leaving the pari passu clause as is exceeds the costs of adopting the modified clauses. The "interpretive shock" of a court giving a private investor the means to force a sovereign nation into default, and the investor actually exercising said power, has become too costly for market participants.[151] Furthermore, the Belgian Court's decision is no longer an "aberration" and a one-time occurrence.[152] The formulation of the original pari passu clause has repeatedly been shown to be flawed, and there is no longer any reason to try and protect contracts with those clauses.

The exogenous reasons surrounding the *Peru* litigation are no longer present after *Argentina*. Sovereign nations are now more exposed than ever to the power wielded by holdout investors. There is no longer any doubt surrounding the meaning of, and the costs associated with, the boilerplate formulation of the old pari passu clause. Therefore, there are few risks borne by adopting the modified pari passu clause, and there is a sudden rush for market participants to get themselves out of their precarious situations.

C. What to Expect Next

1. Further Litigation of the Pari Passu Clause

Despite the power afforded to holdout investors in *Argentina*, litigation of the pari passu clause is not complete.[153] To fully appreciate the scope of the *Argentina* decision, it is necessary to examine the Second Circuit's decision is greater detail. The pari passu clause in Argentina's FAA Bonds was phrased as follows:

> [t]he Securities will constitute . . . direct, unconditional, unsecured and unsubordinated obligations of the Republic and shall at all times rank *pari passu* without any preference among themselves. *The payment obligations of the Republic under the Securities shall at all times rank at least equally with all its other present and future unsecured and unsubordinated External Indebtedness* . . . .[154]

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150 *See generally* Roubini, *supra* note 5.
151 *See generally* Varottil, *supra* note 23, at 132.
152 *See generally* Choi, *supra* note 17, at 1137-38.
153 *See* IMF, *supra* note 19, at 10.
154 NML Capital, Ltd. v. Republic of Argentina, 699 F.3d 246, 251 (2012).

The Second Circuit concluded that those two sentences of the pari passu clause created two separate obligations.[155] "The first sentence . . . prohibits Argentina, as bond *issuer*, from formally subordinating the bonds by issuing superior debt."[156] In addition, "[t]he second sentence . . . prohibits Argentina, as bond *payor*, from paying on other bonds without paying on the FAA Bonds."[157]

The decision of the Second Circuit adopted the "ratable payment" interpretation introduced by the Lowenfeld affidavit in *Peru*.[158] Still, the court's decision may be somewhat narrow in scope.[159] The Second Circuit merely affirmed the district court's decision that Argentina breached its contract with bondholders by its "course of conduct" and "extraordinary behavior."[160] Future litigation will be needed to determine the meaning of "course of conduct" and the "behavior" necessary to constitute a breach of contract.[161]

Nevertheless, the *Argentina* decision was still sufficient to initiate the rapid change seen in sovereign debt contracts. "[M]ost international sovereign bonds issued after 2000 have *pari passu* clauses that include language that is functionally similar to that in the relevant Argentine bonds."[162] Even though future cases will likely determine the breadth of the "course of conduct" necessary to breach the pari passu clause, "this is the first instance in which a district court order triggered a sovereign

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155 *Id.* at 258-59.

156 *Id.* at 259.

157 *Id.*

158 *See supra* pp. 10-11; IMF, *supra* note 19, at 11.

159 *See id.*

160 Argentina breached the contract in two ways:

> In the first place, Argentina breached the clause by "persisting in its refusal to satisfy its payment obligations" currently due to the holdout creditors—while making payments currently due under the restructured bonds. Secondly, Argentina breached the clause when it enacted the "Lock Law" and "Lock Suspension Law" which precluded the authorities from offering more favorable treatment to the holdouts than what it offered to the restructured bondholders.

See id.

161 *Id.* If the "course of conduct" requires the sovereign to adopt legislation similar to Argentina then scope of the Second Circuit's decision will be rather narrow. However, if "course of conduct" refers to the payments on the restructured bonds, the impact of the decision will be much greater. For a further discussion on the upcoming litigation, s*ee* IMF, *supra* note 19, at 11-13; *see also* Joseph Cotterill, *Pari passu: judgment day*, FT ALPHAVILLE (Jun. 27, 2013, 9:45 AM), http://ftalphaville.ft.com/2013/06/27/1543522/pari-passu-judgment-day/ (discussing the significance of *Exp.-Imp. Bank of the Republic of China v. Grenada* to future pari passu litigation); *see also* Exp.-Imp. Bank of the Republic of China v. Grenada, No. 13 CIV. 1450 HB, 2013 WL 4414875, at *1 (S.D.N.Y. Aug. 19, 2013).

162 *See* IMF, *supra* note 19, at 11.

default by barring a sovereign from paying on debt obligations . . . it was willing and financially able to meet."[163] Now, other sovereigns have witnessed a nation default on debt that is functionally equivalent to their own. That default is likely the reason why the new ICMA model contract clauses have been adopted so quickly.

2. Pari Passu as a Matter of English Law

Both *Peru* and *Argentina* dealt with the pari passu clause as a matter of New York law.[164] Yet, a large percentage of outstanding sovereign bonds are governed subject to English law.[165] Still, "[t]here is no clear English judicial precedent on the interpretation of the *pari passu* clause."[166]

In 2005, the Financial Markets Law Committee ("FMLC") published a report, which concluded that the pari passu clause would follow the "ranking" interpretation as a matter of English law and not the "ratable" interpretation.[167] "It is . . . strongly asserted that the [ratable] payment interpretation of the *pari passu* clause is unsupportable as a matter of English law except where the clause is very clearly drafted to achieve this effect."[168] Following the decisions of the Second Circuit and the Supreme Court in *Argentina*, the FMLC reiterated its position that "English Courts would . . . likely take a different approach . . . and in particular would likely regard the remedy of specific performance as unsuitable."[169]

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[163] Marco E. Schnabl & Jordan C. Wall, *A Question of Behavior: Foreign Sovereign Debt Restucturing Before US Courts*, SKADDEN, ARPS, MEAGHER & FLOM LLP (Jan. 2015), http://www.skadden.com/insights/question-behavior-foreign-sovereign-debt-restructuring-us-courts.

[164] *See* Elliott Associates, L.P. v. Banco de la Nacion, 194 F.3d 363 (1999); *see* NML Capital, Ltd. v. Republic of Argentina, 699 F.3d 246 (2012).

[165] IMF, *supra* note 19, at 13 ("[S]overeign bonds governed by English law represent approximately 40 percent of the outstanding stock in notional value.").

[166] *Id.*

[167] *Id.*; *see also* FMLC, *supra* note 74, at 22.

[168] FMLC, *supra* note 74, at 22. The FMLC provided three reasons for its assessment that English Law would differ from New York law in regards to the pari passu clause. *See id.* at 2. First, the "ratable" interpretation would offend the "business commonsense" principle used by English courts when construing a contract. *Id.* Second, based on the principles of English rules of contract construction, words should be given their "ordinary and natural meaning." *Id.* The most literal interpretation requires a "rank" of claims, and does not require pari passu "payment." Third, analysis of English case law provides persuasive authority against the "ratable" interpretation. *Id.*

[169] *Role, Use and Meaning of Pari Passu Clauses in Sovereign Debt Obligations as a Matter of English Law*, FMLC http://www.fmlc.org/uploads/2/6/5/8/26584807/fmlc_memorandum_on_pari_passu_clauses.pdf (last visited Feb. 15, 2015, 4:00 PM).

Should the contested interpretation of the pari passu clause appear in English courts, the FMLC report should prove to be very persuasive by serving a similar purpose as the Lowenfeld affidavit in *Peru*. "There is almost no risk that English courts, faced with similar facts to *NML v Argentina*, would adopt the 'payment' interpretation."[170] Still, it would be risky for English contracting parties to continue to use the boilerplate pari passu clauses.[171] There will always be risk associated with any sort of litigation and it is impossible to guarantee that a judge will not follow the *Argentina* decision.[172] Also, the process of engaging in such litigation, alone, can prove costly and foreign market participants may still feel exposed using the original boilerplate clauses.[173]

When Choi and Gulati conducted their research on boilerplate evolution in sovereign debt contracts, they also studied the impact of an "interpretative shock" on English-Law bonds.[174] They observed that English market participants did react to shocks in the New York market, but that the innovation was considerably smaller than what was occurring in New York.[175] The big change that took place in New York was the shift from UACs to CACs; but, "the English market was already using CACs when the New York market shocks occurred."[176] Therefore, it is not entirely clear how the English market should react when the boilerplate clauses, that received the interpretive shock, differ very little between English and New York law.[177]

Although it has been widely accepted that an English court would not accept the Second Circuit's interpretation of the pari passu clause in *Argentina*, it would not be surprising if the English market modified its boilerplate pari passu clauses as well. Nevertheless, it is unlikely that new sovereign bonds will increasingly adopt English law in their choice of law provisions instead of New York law. The new modifications to the pari passu clause subject to New York law make explicit the intentions of the contracting parties to adopt the "ranking" interpretation; and therefore, the reasons for changing the governing law provisions to a

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170 Lachlan Burn, *Pari passu clauses: English law after NML v Argentina*, 9 CAPITAL MARKETS LAW JOURNAL 2, 9 (2014), http://cmlj.oxfordjournals.org/content/9/1/2.full.pdf+html.

171 *See id.*

172 *Id.*

173 *Id.*

174 Choi, *supra* note 13, at 30-35.

175 *Id.* at 31.

176 *Id.* at 30.

177 An example of an English-Law pari passu clause (for the Republic of Estonia) is as follows: "The Notes and Coupons rank and . . . will rank *pari passu*, without any preference among themselves, with all other outstanding unsecured and unsubordinated obligations of the Issuer, present and future." FMLC, *supra* note 74, at 19.

more favorable jurisdiction are obviated.[178] The main reason for a foreign-law choice of law provision in a sovereign debt contract is to prevent the issuer from changing its domestic laws in order to get out of an unfavorable provision in the contract.[179]

Furthermore, there are other reasons why parties choose New York law.[180] "New York has a well-developed body of commercial law[,] . . . its courts are considered both impartial and experienced in resolving disputes[,] . . . and . . . many of the lenders to foreign sovereign debtors are based in New York."[181] Therefore, sovereign bonds issued subject to English law may change to reflect the Second Circuit's decision in *Argentina*, but it is unlikely that there will be an increase in sovereign bonds issued subject to English law.

IV. CONCLUSION

When new boilerplate clauses are adopted in sovereign debt contracts, smaller market participants are first to adopt the changes.[182] Larger market participants will only shift when it is evident that a new standard is clearly underway.[183] Peru, Mexico, Kazakhstan, and Vietnam have already issued new debt using ICMA's model clauses.[184] However, unlike historical changes to boilerplate contracts, it has not been individual countries that are innovating the new clauses.[185] ICMA and the IMF, both undoubtedly large market participants, have modified the pari passu clauses.[186]

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178 *See* IMF, *supra* note 19, at 15.

179 *See* Andrew Clare & Nicholas Schmidlin, *Impact of Foreign Governing Law on European Government Bond Yields*, SSRN (Mar. 8, 2014), http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2406477, at 9. In fact, this is what the Greek Parliament did when it approved Law 4050/2012 on February 23, 2012, aka, the "Mopping-Up Law." *See* Melissa A. Boudreau, *Restructuring Sovereign Debt Under Local Law: Are Retrofit Collective Action Clauses Expropriatory?*, 2 HARV. BUS. L. REV. 164, 165-66 (2012). "Instead of directly modifying contractual language, the Mopping-Up Law would change local law to effectively incorporate a collective action clause in all untendered local-law bonds." *Id.* at 168. For these reasons, strong evidence suggests that "foreign law bonds should trade at a premium to bonds governed by local law since they are harder to restructure." *See* Clare, *supra* note 179, at 32.

180 *See* George Weisz et al., *Selected Issues in Sovereign Debt Litigation*, 12 U. PA. J. INT'L BUS. L. 1, 4 (1991).

181 *Id.*

182 *See* Choi, *supra* note 13, at 21.

183 *Id.* at 22.

184 *See* Gelpern, *CACs v. 2.0*, *supra* note 108; *see also* Gelpern, *ICMA CACs*, *supra* note 108.

185 *See* Choi, *supra* note 13, at 21.

186 *See* Gelpern, *supra* note 35; *see also* IMF, *supra* note 19.

The Second Circuit decision in *Argentina v. NML* and the subsequent debt default by Argentina is arguably the strongest "interpretive shock" that the pari passu clause has ever received. The pari passu clause has suddenly become a "weapon" that holdout investors are willing to use. Unlike *Peru*, it would make little sense for market participants to continue their coordinated litigation strategy. The pari passu clause has been demonstrated to be dangerous and it presents an immediate threat to insolvent sovereign nations. No reasons exist, either endogenous or exogenous, to have a long waiting period until large-scale adoption of the new pari passu clauses. Change is clearly underway, and it can be expected to see further large-scale market adoption of the reformulated pari passu clauses in sovereign debt contracts.